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department
of economics**

LATIN AMERICA IN THE LIGHT OF REPORTS ON DEVELOPMENT

- I. REPORTS ON AID
- II. WHAT CAN BE DONE ABOUT LATIN AMERICAN DEVELOPMENT

P. N. Rosenstein-Rodan

Number 66

December, 1970

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P.N. Rosenstein-Rodan (M.I.T.)

I. Reports on Aid

1). Progress in understanding--deterioration in action.

"Quand un philosophe vous répond, vous commencer à ne plus comprendre du tout ce que vous avez demandé..."

(Andre Gide, Palludes)

Development and aid receive nowadays a massive intellectual attention. Apart from individual books and articles a dozen group reports have been published during the last few years.* These reports follow the massive work and documentation of the UNCTAD I and II, as well as previously written individual reports.**

- * 1. Development Assistance in the New Administration, The President's General Advisory Committee on Foreign Assistance Programs, (James A. Perkins, Chairman) October 1968.
- 2. A New Conception of U.S. Foreign Aid, National Planning Association, March 1969. (The best and most sensitive among the U.S. reports).
- 3. Assisting Development in Low Income Countries: Priorities for U.S. Government Policy, C.E.D., September 1969.
- 4. U.S. Foreign Assistance in the 1970's: A New Approach, (Rudolf A. Peterson, Chairman) March 1970.
- 5. Report of the Task Force of the National Association of State Universities and Land-Grant Colleges on Technical Assistance, Michigan 1969.
- 6. Draft report on The Role of Europe Member States in the Second U.N. Development Decade, Council of Europe Consultative Assembly, Committee on Economic Affairs and Development, Strasbourg, 18 December 1969.
- 7. A Study of the Capacity of the United Nations Development System, report by Sir Robert Jackson, U.N., Geneva 1969.
- 8. Partners in Development (Lester B. Pearson, Chairman) September 1969. (The most comprehensive report of the Commission on International Development, sponsored by the World Bank. See also 40 papers on subject matters treated in this report presented at the Columbia University Conference on International Economic Development, Williamsburg and New York, February 1970.

9. Report of the U.N. Committee for Development Planning, (Professor Jan Tinbergen, Chairman), January 1970.

On Latin America:

10. Quality of Life in the Americas, report of a U.S. Presidential Mission by Nelson A. Rockefeller, November 1969.
11. Latin American Consensus of Vina del Mar, Pan American Union, May 1969.
12. Foreign Aid: A Report on the Reports, Willard L. Thorp, Foreign Affairs, April 1970 (reviewing the above ten reports).
13. Transformación y Desarrollo, La Gran Tarea de América Latina, Raul Prebisch (report presented to the IDB, April 1970).

**Among these are:

1. United Nations: Measures for the Economic Development of Underdeveloped Countries, New York 1951.
2. Max F. Millikan and W. Rostow, A Proposal: Key to an Effective Foreign Policy, New York 1957.
3. The Objectives of United States Economic Assistance Programs, a study by the Center for International Studies, M.I.T., for the Special Committee to study the Foreign Aid Program, U.S. Senate, Washington, D. C. 1957.
4. Paul G. Hoffman, One Hundred Countries, One and One-quarter Billion People, Washington, D.C. 1960.
5. P.N. Rosenstein-Rodan, "International Aid for Underdeveloped Countries," The Review of Economics and Statistics, Cambridge, Mass. 1961.
6. J. Tinbergen and Centre de Documentation du Comite d'Action pour les Etats Unis d'Europe, La Communaute Europeenne et Les Pays Sous-Developpes, May 1959.
- 7 and 8. The first four have been summarized in The Capital Development Needs of Less Developed Countries, U.N., New York 1962. The estimates of capital requirements of 1-5 have been compared taking account of various assumptions and methodology in a summary table in, Determining the Need for and Planning the Use of External Resources, U.N. Conference on Technological Progress, Geneva 1965.
9. La Politique de Cooperation avec les Pays en Voie de Developpement ("the Jeanneney Report"), Paris, July 18, 1963.
10. Hollis Chenery and Alan Strout, "Foreign Assistance and Economic Development," American Economic Review, September 1966.
11. See also the comparison of six estimates of global needs for development assistance in the early seventies in Table 4, p. 35, of the Perkins report.

12. A.I.D., Principles of Foreign Economic Assistance, Washington 1963 and 1966.
13. F.M. Coffin, Witness for Aid, Boston 1964.
14. Foreign Aid Through Private Initiative, Report of the Advisory Committee on Private Enterprise in Foreign Aid, 1968 (see also The Watson Committee report, A.I.D., 1965).
15. I.M.D. Little and J.M. Clifford, International Aid, Chicago, 1966.
16. G. Ohlin, Foreign Aid Policies Reconsidered, O.E.C.D., Paris, 1966.
17. Effective Aid, Report of an International Conference held jointly by the Ditchley Foundation and the Overseas Development Institute, London, 1967.
18. J. Pincus, Trade, Aid and Development, The Rich and Poor Nations, New York, 1967.
19. R. N. Gardner and Max F. Millikan (eds.), The Global Partnership: International Agencies and Economic Development, New York, 1968.
20. R. F. Mikesell, The Economics of Foreign Aid, Chicago, 1968.
21. Max F. Millikan, The U.S. and the Low-Income Countries, in Agenda for the Nation, Brookings Institution, Washington, 1968.
22. The Role of Popular Participation in Development (Hapgood, ed.), M.I.T. Press, 1968.
23. Joan M. Nelson, Aid, Influence and Foreign Policy, New York, 1968.
24. O.E.C.D., Resources for the Developing World, The Flow of Resources to Less Developed Countries 1962-1968, Paris 1970.
25. R. Asher, Development Assistance in the Seventies, Brookings Institution, Washington 1970.
26. J. Bhagwati, Amount and Sharing of Aid, ODC, Washington, D. C. 1970.
27. G. Myrdal, The Challenge of World Poverty, New York 1970.

These reports reveal a deep comprehension and sophisticated analysis of the development process. There is in most of them a remarkable similarity in conclusions and recommendations. The thinkers' comprehension

maintained (or slightly increased) in the nineteen-sixties, showing that the underdeveloped countries could take advantage of the economic and technological progress and improve their organization of development policy. Further, social and economic improvement is both possible and probable.

This is most amply documented in the Pearson report.

ii) Development is a complex and necessarily slow process.

Construction of a changing society is incomparably more difficult than a reconstruction like the Marshall Plan. It involves changes in attitudes, in social and economic structure, building of new institutions and new forms of organization. To reach the goal of self-sustaining growth is not a matter of a decade, as it was sometimes implied in the exuberant optimism of the early nineteen-fifties, but of one or two generations. It can be envisaged around the year 2000.

iii) Growth of GNP is not the only objective. Equality of opportunity implying full employment and access to education, better income distribution, openness of society are all part of the "social welfare function." The Alliance for Progress formulated most emphatically the modern development creed in which social and economic progress are an inherent part of the program. Social progress is not anymore the by-product of the end-effect of economic development, but is one of the preconditions and an objective in itself. Without broad participation of the masses new energies would not be mobilized which alone make sufficient effort possible.

This is most sensitively argued in the National Planning Association report, which adds the warning that for that reason an exact assessment of performance is difficult to establish. Different countries may attribute

different weights to different objectives and may reach it in different ways. The Pearson report agrees that there are different objectives of social and economic policy, "but in practice any country which is meeting the tests...(of adequate and sustained increases in the ratio of domestic savings to national income and in the ratio of exports to imports) is likely to be meeting most of the others..." (p. 132). The Prebisch report emphasizes the goal of full employment and better income distribution more forcefully than any of the other reports and works out the strategy of development needed for its realization. It points out that the gap between the rich and the poor is widening not only between countries but also within most of the underdeveloped countries.

The programming problem of the area of complementarity and substitutability of economic and social ends, the trade-offs between them in either one or several periods is not discussed, however, in any of the reports.

iv) The rationale of aid is not questioned in any of the reports. The basic answer is a moral one: "it is only right for those who have to share with those who have not." While it will not win allies or gratitude, nor assure political stability it corresponds in the long run to an enlightened national interest of the developed countries, who want to live in a better world. If we speak of an international community we have to contribute to the building of it. The eloquence of the Kennedy days is missing, but no doubts are expressed in any of the reports. The aim of aid is not a continuous redistribution of income, but of helping in development, helping those who help themselves to reach self-sustaining growth.

v) How much growth? The Pearson report assumes that a 6% rate of growth is possible. The Tinbergen report projects a 6% rate for 1970-1975 and a 7% rate for 1975-1980. The Prebisch report argues that only an extraordinary effort leading to an 8% rate of growth around 1980 can solve the full employment problem in Latin America. Without it a peaceful resolution and a stable solution are impossible.

vi) How much aid? All reports agree that more is needed. The UNCTAD goal of a capital inflow of 1% of GNP has become a "political datum," so that the problem of an equitable sharing of the burden of aid according to a progressive income tax principle (discussed at various DAC meetings) is not discussed. For aid ("official flows") the Pearson report recommends reaching 0.7% of GNP by 1975; the Tinbergen report 0.75% by 1972; the Perkins report recommends a restoration of the 1965 proportion of a capital flow of 1% of national income, while the CED report recommends a 1% of GNP capital flow after 1970. The Peterson report alone abstains from recommending a quantitative target but stresses that "the downward trend in U.S. development assistance appropriations should be revised."

Aid is a system of measures which normal market mechanism cannot provide. All reports (with least said in the Perkins and Peterson reports) recommended accordingly that official flows should be offered at concessional terms as grants or loans at low rates of interest, long maturities and grace periods, so as to avoid an undue burden of indebtedness. "The debt burden of many developing country is now an urgent problem. It was foreseen, but not faced a decade ago" (Peterson Report, p. 12). The Gray Committee report

in 1951 already emphasized the need for grants and soft apart from hard loans. DAC in 1965 and 1969 called for softening of terms in three ways: either i) by providing a very large share (70%) of assistance in the form of grants; or ii) by providing a high proportion of grants or loans which individually carry a large concessional element; or iii) by providing a mix of grants and loans on various terms which, taken together, contain a large average concessional element. The CED report recommends "more flexible terms of lending (softer terms where necessary and harder where appropriate)... with "a reduction of the prescribed interest rates" (p. 44). - The Pearson report recommends "that the terms of official development assistance loans should henceforth provide for interest of no more than 2 per cent, a maturity of between 25-40 years, and a grace period from 7-10 years" (p. 169).

One way to soften terms of lending is proposed by the Pearson report recommendation "that donor countries commit the equivalent of one-half or more of the interest payments due them on official bilateral loans from developing countries to the World Bank to subsidize the interest rates on some Bank lending. - Other variants of an international Horowitz proposal have been discussed at various international meetings.¹

The commitment of interest (and possibly part of amortization) payments on official loans to bilateral or multilateral lending agencies can also be a way to assure continuity of lending.

While future official flows at softer terms should help to prevent

¹ Italy uses budget appropriations for covering the loss due to interest rates on loans which are lower than the rates at which Government issues its bonds for that purpose. Unfortunately that provision in the Legge Martinelli is confined to loans up to only 10 years maturity.

an excessive debt burden, past borrowing created in several countries a grave problem of debt service payments. Debt renegotiation and conversion loans are accordingly needed--and should be counted as part of the contribution to aid. Debt renegotiation is a complicated operation. It is recommended that the problem be studied by the World Bank and IMF was to establish objective criteria for debt renegotiation (CED and Pearson reports).* The Rockefeller report adds a condition to the moratorium device in debt rescheduling. The equivalent in local currency of the amount of the debt which is postponed for a period of years is to be paid to a fund to be used for development purposes. The whole debt service problem should be studied by C.I.A.P. and discussed with I.D.B. and other international lending institutions.

A gradual untying of aid is recommended. The Pearson report suggests a series of steps which make a general untying easier without reducing the overall flow of aid. Immediately, however, aid givers should permit aid financed procurement in other developing countries. Costs arising from the tying of and to the use of donor shipping should be excluded from statistics of official development assistance (p. 179). The Rockefeller report accepted the Consensus of Vina del Mar request to drop the "additionality clause" in the aid to Latin America.

vii) Continuity of aid is as important as the amount was claimed already in the 1954 report of ECLA (Junta Preparatoria for the Conference

* The problem of debt renegotiation as part of providing aid will be further discussed in the Latin American context (see II...).

of Quitandinha).* Without it adequate planning is impossible. All reports accordingly recommend it. The Perkins report recommends two years appropriations. The National Planning Association report says: "...An essential prerequisite for a more effective U.S. development assistance effort is continuity of authorization and greater calculability of funding... The Development Loan Fund (should be revived) with an indefinitely continuing authorization or, if not, with authority to operate for a specified time period of not less than five years." (p. 10-11). "Congress would not have to authorize foreign aid anew each year and appropriate all of the money required for it, as must now be done. The present procedure is an abuse of the legislative process. It is unrealistic, we believe, for already burdened legislators to be expected to review seriously a whole complex of foreign aid activities each year...Even with the best will in the world, the present procedure invites a kind of rhetorical activism from the Congress which has encumbered the U.S. foreign aid effort with a multitude of often unrelated legislative restrictions...defeating the long-range development purposes that most of U.S. aid is intended to serve...Congress would have the opportunity periodically to make a thorough review (on a function to function basis). This would permit a much more substantive and rational reexamination by the Congress of the constituent parts of the U.S. foreign aid effort than now occurs" (p. 23). The C.E.D. report recommends that authorizations for bilateral lending should be made for periods of at least three years and

* International Co-operation in a Latin American Development Policy, (E/CN, 12/359).

appropriations for a minimum of two years. The Peterson report would achieve the continuity of aid by the creation of U.S. International Development Bank, with "assured sources of financing, including authority to borrow in the public market." That is a part of a new institutional framework including in addition a U.S. International Development Institute for technological research, the Overseas Private Investment Corporation (OPIC) also recommended by the C.E.D. report* and U.S. International Development Council--designed to make aid more effective and destined to satisfy the Congress's mood for change irrespective of the functional need for it. For that reason even the Perkins report recommends a change in name: AID should become DCF (Development Corporation Fund) although it states that "A.I.D. has accumulated a store of experience and professionalism that has enabled it to be an innovating leader in the world system of development assistance" (p. 16). Apart from satisfying the U.S. temperamental taste for reorganization the institutional change might at least provide for greater continuity of aid and for simplifying "as much as is politically possible the present brier patch of specific legislative requirements, which now require, for example, 77 statutory conditions for loan to build rural roads in Liberia" (Perkins report, p. 17). The Rockefeller report also recommends that "development or program loans should be made on a three to five years commitment basis, through the proposed Institute of Western Hemisphere Affairs" (p. 76), and that the Pelley, Conte, Hickenlooper, Symington and Roess amendments be

* See also X.

suspended or modified (p. 77). The Pearson report recommends: "All aid-givers should consider extending appropriation periods to at least three years, and permitting appropriated funds to be carried forward for several years" (p. 171).

viii) Economic and military assistance should be separated. All reports, with the exception of the Rockefeller report agree on that. "Governor Rockefeller's concern about the supposed communist threat is anachronistic..." (A. Lowenthal: "Alliance Rhetoric versus Latin American Reality," Foreign Affairs, April 1970, p. 502).

ix) Technical assistance should be integrated a) within the U.N. system, according to the Jackson report; b) between aid lending and technical assistance activities (including pre-investment and feasibility studies). This is certainly needed since "it is apparent that the flow of technical assistance has tended in the past to be more determined by what was available than by what the recipient countries really needed" (Council of Europe Report, p. 48). Only the National Planning Association and the Peterson reports recommend separate agencies for lending and technical assistance. On the face of it fragmentation is proposed where more integration is needed. But the Nat. Ass. write: "We believe that the removal of technical assistance and private enterprise activities from AID would not seriously impair coordination of the different types of aid. Located as they must be in Washington, both the Technical Assistance and Development Research Institute and the Private Enterprise Development Corporation would be able to maintain continuous liaison at the operating level with AID and other U.S. agencies

concerned with development. The presence on their boards of directors of the administrator of AID would provide a formal channel through which inconsistencies in policies could be resolved and disagreements settled through top-level negotiations...cooperation between the two organizations (is possible) without impairing the effectiveness of the former or the independence of the latter" (p. 24). Robert Asher also says: "The theoretical advantages of having one agency responsible for technical assistance, investment guarantees, program-lending, and project lending have to a considerable extent remained theoretical" (op. cit., p. 144. On technical assistance see ibid. pp. 148-153). Knowing how difficult it is to coordinate activities of two different departments of the same organization, not to mention those of different organizations, we may express some doubt about the usefulness of separating technical assistance from lending agencies. It is to be remembered, however, that the Peterson U.S. International Development Institute is to "seek new breakthroughs in the application of science and technology to resources and processes critical to the developing nations" (p. 5) i.e., for long-run technological research. Normal technical assistance activities could be provided by the U.S. Development Bank, if this interpretation is correct. - The Pearson report recommends that multilateral and bilateral technical assistance be more closely integrated with capital assistance.

- x) Private Foreign Investment should be encouraged by fiscal devices as well as investment insurance--but it is recognized that it cannot alone substitute for aid. The creation of OPIC (Overseas Private Investment

Corporation) is recommended by the CED and the Peterson report (with a similar proposal for Latin America in the Rockefeller report). It was also recommended by the Watson Committee Report, 1965, and by A.I.D., 1968, "The report is singularly oblivious of the problems connected with private foreign investment. Its underlying assumption seems to be that the more U. S. private investment is pumped into the less developed countries, the better off everyone will be."... It should not be "a zealous investment-promotion agency that will be inviting expropriations costly to the U.S. government (diplomatically as well as financially), partly because they are relatively costless to the insured, protected private investor." (R. Asher, op.cit., p. 196). The Pearson report does not enter into a systematic discussion of the cost-benefit ratio of private investment and an examination of its relative role and "topography" in the development field. While it does not say anything wrong it does not say very much and certainly not enough. The C.I.A.P. papers, the IDB round table conference in Bogota (April 1968) using the C.I.A.P. papers as well as the Prebisch report go much deeper into the analysis of this problem.*

xi) Trade Policy for Development. All reports with the exception of the Perkins, C.E.D. and National Planning Association recommend measures for the expansion of trade, including reduction (or preferably removal) of quotas and restriction, temporary non-reciprocal tariff preferences, for industrial products and support for regional preferential-tariff areas or common markets. The lesson of UNCTAD has been absorbed in theory at least if not yet in practice. "The trade gap concept was never formally accepted

* The problem of private foreign investment in Latin America will be discussed separately in II....

by the developed countries as a reference criterion. For a start, as pointed out by the Pearson report, trade cannot be a substitute for development aid, a principal feature of which is a net transfer of real resources. On the other hand, developing countries' aid requirements stem in part at least from their insufficient export earnings and the difficulties in increasing them. In the long run, it is only if they succeed in stepping up their exports to industrial countries and in substituting domestic production for imports from those countries, that the developing countries will be able to break their present dependence on external aid" (Council of Europe report, p. 41). "Developing countries cannot be expected to reach the point of financing their own development unless they are given the opportunity to earn the means for doing so through an increase in their exports" (Peterson report, p. 22). - It follows logically that aid would have to be larger, softer, and extended over a longer period if facilities for trade expansion were not offered. In this sense trade and aid can be considered as (albeit imperfect) substitutes.

More than four-fifths of the developing countries consist still of primary products which suffer from protectionism (not only tariffs but quantitative restrictions) in the developed countries as well as from the fact that demand for imports grows much more slowly than for industrial products. The Pearson report distinguishes between non-competing (coffee, cacao, tea) and competing primary products among which minerals and metals move relatively freely while among tropical products(sugar, rice, fats, and oils),among new materials (cotton and tobacco) , among temperate

foodstuffs (cereals, meat and dairy products) suffer from extreme protectionism in the form of quantitative restrictions. In a pessimistic mood as to prospects of complete liberalization in this field the Pearson report proposes as a second-best solution "that developed countries draw up plans in respect of protected commodities designed to assure that over time an increasing share of domestic consumption is supplied by imports from developing countries" (p. 85).

Many primary products suffer from price fluctuation. Commodity agreements should be designed to reduce short-term price fluctuations while maintaining long-term flexibility. This might imply diversification of products but its aim need not be a general permanent improvement in the terms of trade. Where appropriate buffer-stocks should be financed (Pearson Committee report, p. 86), and unanticipated shortfalls in exports^{*} should be compensated by supplementary finance which would be supplementary to, not a substitute for, existing forms of aid. - Commodity agreements, buffer stocks and supplementary finance should be considered in a logically coordinated way. Commodities that cannot be stored (e.g. bananas) in buffer stocks should receive other forms of support. Where an effective commodity agreement and/or a buffer-stock is operating less, or no, supplementary finance is required. The reports do not give this chapter a sufficiently systematic treatment.

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* Isaiah Frank has suggested that not only unanticipated shortfalls in exports but also unanticipated increases in import requirements caused by draught or other adverse conditions beyond a country's control should be covered. ("Foreign Trade Policies and Latin American Development", statement 1 March 1968 before the Senate Foreign Relations Committee, p. 14.)

The greatest expansion in exports, however, will materialize in industrial products. A substantial proportion of manufactured exports is limited by quotas." Excluding petroleum products, base metals and ships, no less than 30 per cent of manufactured goods are subject to quantitative restrictions. Their abolition could perhaps benefit underdeveloped countries more than non-reciprocal tariff-preferences on other goods. The Kennedy round tariff reductions seem to benefit the developed countries more than the developing ones. The tariff structure is rigged against the less developed countries. The nominal tariff rates usually understate substantially the true effect of tariffs. "The effective protection afforded to processing of raw products with free entry of the raw material may be very high indeed, because the cost of processing may be small by comparison with the cost of the raw material... The clear implication of the theoretical considerations and empirical evidence is that, despite impressions to the contrary derived from contemplation of nominal tariff levels, preferences in developed-country markets for exports of manufactures and semimanufactures might well exercise a powerful influence in expanding the export earnings and promoting the industrialization of the less developed countries."^{*}

Accordingly, non-reciprocal temporary tariff preferences are recommended. The practice is still different, however, "At the March 1969 meeting of the OECD member governments were to submit lists of products on which they were prepared to consider granting preferences, but the U.S.

* H.G. Johnson: Economic Policies Toward Less Developed Countries, Brookings Institution, Washington 1967, pp. 90/91 and 173.

failed to produce a list and could only say that the new administration needed more time for a review of American trade policy in all its aspects. Other OECD members were glad to have an excuse for delay, and the momentum resulting from President Johnson's 1967 endorsement of the proposal in Latin America is being lost."*

The Pearson report recommends general non-reciprocal temporary tariff-preferences to all underdeveloped countries. The Peterson and Rockefeller reports recommend the same but add that if agreement on it cannot be reached preferences should be given to "all developing countries except those that choose to remain in existing preferential agreements." (Peterson report, p. 23). These "vertical" preferences - only as long as no agreement on "horizontal" ones can be reached - have become a somewhat "theological" argument in Latin America. It is not being considered whether their temporary introduction might not induce Europe to change its present practice. It is interesting to note the Delphic statement by the Council of Europe report: "The existing preference system between the EEC and the 18 states of Africa and Madagascar and between the United Kingdom and the Commonwealth should not be allowed to stand in the way of the establishment of a general system of preferences. On the other hand, the existing institutional arrangements for co-operation with particular groups of developing countries historically linked to Europe should not be called in question as long as equally effective arrangements have not been set up at the world level." (p. 54 [x]). "However, that may be, the contribution of

* R. Asher, op. cit., p. 162.

Europe to the Second Development Decade cannot wait on the future progress of the Community. The member states of the Council of Europe together represent the second pillar of the industrialised world after the United States. At a time when the willingness of the United States to pull their weight in the field of development co-operation seems in doubt, it becomes even more important that the European countries should give a lead." (p. 55, #5).

All reports agree further to favor expanding trade among developing countries in the form of regional or subregional preferential tariff areas or common markets.

Apart from trade policy itself, the conclusion of all the reports is that trade and aid should not be considered separately. "It has become clear that the development of the poorer countries will also require important adjustments in the industrialized countries, to which the latter are reluctant to submit. Indeed, aid has sometimes been termed a 'soft option' compared to the measures which are indicated in the field of trade" (Pearson report, p. 80). - "Policies in international trade, investment and finance can no longer be formulated without considering their consequence for development. Action to be taken in those areas calls for international co-operation" (Peterson report, p. 12).

xii) Multilateralization of aid.* International cooperation for building stable and self-reliant societies implies a partnership. Aid

* The subject will be more amply treated in II. Here we provide only a brief summary of what is said in the reports.

receiving countries should decide on the objectives of their development programs and on the mix of policy instruments apt to realize them, but the aid-giving partners have the moral right (and the political constraint of their public opinion) to check whether the purposes of aid are being met.* National effort is the main source and basis of development, aid is only a marginal, albeit crucial, supplement. If aid is a sort of international income tax then taxpayers (however small the tax) have the right to examine whether the administration of the common undertaking fulfills the mutually agreed upon conditions of the international social contract and notably whether aid is a supplement to, not a substitute for national effort. The very discussion by one country of what another country is doing or should do invariably raises objections that national sovereignty is being infringed. It cannot be said either that the purposes of developmental aid were always clearly formulated, neatly separated from other objectives and handled with tact and sensitiveness. The concept of international cooperation in development accordingly "began to lose its shine before it had gained any widespread currency." Yet an impartial independent evaluation alone can reconcile the legitimate interests of both parties. All reports agree on that point. The beautifully and sensitively written proposal of a different "aid on long-term trust" approach without any assessment of effort or performance remains the voice of a lonely

* Developing countries...establishing their own priorities, receiving assistance in relation to the efforts they are making on their own behalf" (Peterson report, p. 3).

dissenter.* The Pearson report says: "It is natural, that aid providers are particularly interested in whether recipients make sincere efforts to help themselves, or whether the resources put at their disposal are wasted. However, this interest, unless carefully limited and institutionalized, creates opportunities for friction, waste of energy, and mutual irritation. (p. 127)...The emergence of consortia, consultative groups, and the multilateral procedures of the Alliance for Progress serve very considerably to increase the effectiveness of aid by making it possible for donors, whether bilateral or multilateral, to help recipients develop policies more likely to promote self-sustaining growth. ...This would often be difficult and irritating in a purely bilateral context. It is still difficult but not so irritating or fraught with suspicion when done in a multilateral context" (p. 129). Accordingly all reports recommend a shift of aid finance (and decisions) to multilateral channels--primarily at first to the World Bank who proved its efficiency and has the most ample intellectual and organizational resources and later on as they improve their competence to regional Development Banks. The Rockefeller report, however, specifically

* I.G. Patel: Aid Relationship for the Seventies. - A Comment on the Report of the Commission on International Development, Pearson Conference Document No. 17, Columbia University, February 1970: "The Commission was addressing itself mainly to the Parliament and the public in the aid-giving countries; and it is natural to assume that the time for making a proposal is hardly the time to dilate on the difficulties of marriage or on the need to take a less romantic view of each other. But the occasion is more like the reunion of an estranged couple. A better course may well be to carry on quietly for some time and build around obvious things like the children and the garden. Meanwhile, it can do no harm to read the old letters again or even to turn the pages of the manual on ideal marriage one read with such avidity not so long ago." (p. 13).

mentions IDB, IBRD and CIAP for Latin American activities. The specific form of shifting aid finance to multilateral channels is not discussed. It can be an increase in capital subscription to the World Bank and to Regional Development Banks, a transfer of (one half or more) appropriations (hopefully for several years, not annually) either to the general funds of the World Bank (and other multilateral agencies) or to be administered in a specific fund, or an appropriation of an interest subsidy for bonds issued by these agencies (any variant of the Horowitz proposal); any one form or a mixture of them in different proportions is possible. A transfer of financial resources to multilateral channels is however, at best, only a partial transfer of decisions; that requires additional examination usually undertaken under the headline of coordination of aid (see xiii and II...).

In many cases, especially also in hearings and speeches at the U.S. Congress the shift to multilateralism almost appears as an escape from difficulties, proposing to act like the man, who, in order to cure his wife's promiscuity, threw out the sofa on which she was found in flagranti. The National Planning Association report gives however a sophisticated historical and psychological analysis of the problem: "When, early in the 1950's, the focus of U.S. foreign aid began to shift from Western Europe to Asia, Africa and Latin America, Americans were conscious of a need and an opportunity which they wanted to meet...During the 1950's, not only did the U.S. have to provide the bulk of the capital and technicians required by the underdeveloped countries but, with a few notable exceptions, it also had

to supply much of the sustained initiative, the substantive ideas, the organizational and administrative experience, and the techniques of program planning and project design without which the money and the experts could not have been put to work...This active and directive U.S. approach to development assistance, however, became less necessary for most recipient countries in the course of the 1960's in consequence of the development progress that has so far been achieved (pp. 2-3)...Self-help also implies that the initiatives and decisions countries take about how to use their resources for development must be in the deepest sense their own, not those of Americans...While continuing to provide sound advice to those leadership groups committed to development, the inhibiting effects of U.S. activism have to be substantively reduced. Such a reconciliation is by no means easy, for American activism is not a superficial characteristic...it has very deep roots in American culture...Hence, the U.S. foreign aid effort needs to be structured and administered in ways conducive to a more reactive, rather than active, posture on the part of the officials engaged in carrying it on... Today, an increasingly popular prescription for easing this problem--as well as, it is believed, to obtain other benefits--is to multilateralize the provision of foreign aid. By this is meant transferring to international organizations the responsibility for allocating and dispensing all, or a substantial part, of the resources which the United States is willing to devote to development assistance. Certainly, sound policy advice, insistence on adequate performance standards, and direct involvement in proposing, designing and administering programs and projects are, at least initially,

less resented and less inhibiting of self help and self responsibility when they come from an international agency, in which the recipient countries are also represented, than bilaterally from a large donor nation. For this reason, as explained below, we favor increased use of multilateral means. But multilateralization is not a panacea nor could it be made the sole--or even major--channel for U.S. foreign aid for some time to come." (National Planning Association, p. 6).

In spite of the new mood to transfer aid funds to multilateral organizations it is doubtful whether Congresses who are reluctant to vote a sufficient amount of aid under bilateral administration would vote higher amounts for a multilateral administration out of any national control. If that is so, then the sacrifice of that amount of aid is not worth it, especially since the drawbacks and failings of bilaterally administered international aid can be effectively reduced by a system of "bilateral aid within a multilateral framework" as proposed in a M.I.T. study in 1957.^{1,2} Each nation contributing aid bilaterally would be asked to try to apply internationally agreed criteria for aid and to notify an international or regional coordinating committee of every hard or soft loan contemplated or given to less developed countries.

¹"The objectives of United States Economic Assistance Programs," a study by the Center for International Studies, M.I.T. for the Special Committee to Study the Foreign Aid Program, U.S. Senate, Washington, D.C., 1957.

²The suspension of the Pelley, Conte, Hickenlooper, Symington and Roess amendments would, however, be necessary.

A study on "The Consortia Technique" * points out the progress realized by the technique of consortia. "Their advantage is not only that of mobilizing resources for different countries or agencies but also that of assessing the country's development effort and its strategy as a whole and not limiting its attention to single project analysis...Its main drawback seems to be that it becomes somewhat haphazard and accidental whether each country will in fact receive the suitable amount and composition of aid. This would only be possible if one, some, or all countries were willing to 'underwrite' the residual amount of aid (i.e. the amount required to make up the total lending appropriate for this country)...One form or another of underwriting a 'loan fund of last resort' must logically complement the consortia technique."

The Pearson report reaches this conclusion somewhat obliquely in the case of the World Bank and more explicitly in the case of IDA: "In order to assure that all developing countries whose performances and level of development warrants it receive the development assistance which they can effectively absorb, the resources must be considerably expanded (p.214)... IDA lending should be based primarily on performance and should seek to offset the most serious imbalances of bilateral assistance (p.227). This aim of acting as a "lender of last resort" can be met if "aid-providers increase grants and capital subscription for multilateral development aid programs to a minimum of 20 per cent of the total flow of official development

* P.N. Rosenstein-Rodan, in Global Partnership, International Agencies and Economic Development (N.Y.: Praeger, 1968), p. 223. (Originally written as a paper for the Committee of Nine, July 1963).

assistance by 1975" (p. 215). This would mean a doubling of multilateral flows which at present form 10% of total aid. Not only the World Bank Group but the whole group of international financing agencies could then play the role of "balancing" - i.e. of the "lenders of last resort." They would have to change the still prevailing attitude (or habit of the "project approach" or "project lending") which moves each agency (like each bilateral agency) to "pick the raisins," i.e. to select "better" (higher priority) projects. If the development program is clearly formulated this is largely an optical illusion. The program approach determines what volume of lending i.e. how many projects should be financed. Single project analysis cannot ascertain the criteria of "additionality" or "optimality" i.e. it cannot be seen outside the framework of a development program whether the project constitutes additional or optimal investment. Single projects do not add up to a program. But a program can be--and if the definition of a "project" is wide enough, should be--spelled out in projects. The fear that the lender of last resort will have to finance the lowest priority projects would be unfounded if aid from all sources were properly coordinated.

xiii) Coordination of aid is needed both among donor and within the receiving countries if aid is to be effective and if the relation of partnership is to be credible. Several of the numerous bilateral and multilateral agencies (notable A.I.D. in the U. S. and the World Bank) discuss and survey the countries' development program. The very "multiplicity of agencies leads to much unnecessary duplication of effort..." and for the most part the dispersed nature of reporting of development

progress deprives such reports of influence" (Pearson report, p. 228). More importantly, the absence of clearly established criteria and the suspicion of "strings" attached to aid causes resentment on both sides. An "institutionalization of relationships in ways that minimize the strains inherent in confrontation of rich donor and poor recipient and maximize the self respect of both parties" (Asher, op. cit., p. 103) is called for. Multilateralization does not primarily refer to the forms of administration (national or multinational) but fundamentally to the spirit in which policy is operated and to the criteria of evaluation of development programs by an independent multinational body which conceives the aid effort as a supplement to total national development effort, not to single parts of it, and which offers an operational conclusion on how to allocate external aid resources. The essence of multilateralization consists in a de facto delegation of decisions on aid allocation.

The two relevant questions: i) can national development effort be measured and can on that basis valid criteria of aid allocation be established? and ii) who should apply these criteria and pronounce the verdict? are not treated consistently and lucidly in any of the reports. The Pearson report correctly mentions that such criteria can be established, that exact measurement of each country's comparative development effort is not required and that judgment on whether this effort is excellent, mediocre or insufficient can be arrived at without hesitation. As a self-respect measure the Pearson, Peterson, and Rockefeller reports recommend that the monitoring of aid effort should apply both to the contributing and receiving

countries. The Pearson report recommends that the bulk of the coordinating function should be performed by the World Bank, the Tinbergen report recommends ECOSOC of the U.N. and the Jackson report recommends that UNDP should coordinate the technical assistance.*

The Pearson report proposes regional groupings "a la C.I.A.P." and describes the four principal functions that coordinating machinery should perform:

"First, it should relate aid and development policies to those concerned with trade, monetary policy, and private capital movements to avoid possible nullifying of the beneficial effects of aid by unfavorable trends in these other fields.

Second, it should move toward standardized assessments more clearly related to generally accepted performance criteria. Such reviews should be acceptable to all relevant institutions, rendering it unnecessary for every agency to make separate assessments. This would contribute both to the aid relationship and to the efficiency of the resource transfer. Even more important, the fact that broadly consistent standards would be applied to the performance of all developing countries should improve public confidence in aid.

Third, on the basis of these assessments clear, regular, and reasonably authoritative estimates of development objectives and aid requirements could be made. The estimates should be made on a standardized basis and at a level of detail designed to coincide with appropriation processes in donor countries.

* -----
See insert, p. 27a.

*The main difficulty is to establish a coordinating agency which would have the confidence and command respect from both the lending and borrowing countries. The proposal in the 1950's to create SUNFED as a capital-lending agency within the U.N. was turned down because of lack of confidence in the U.N. administrative ability and the suspicion that it would be biased in the receiving countries' favor. The same is still true to some extent about CIAP and the Regional Development Banks. On the other hand developing countries still suspect that the World Bank (as well as D.A.C. and OECD) is too "closely linked to the big and wealthy powers." An impartial independent evaluating body like the Committee of Nine within the Alliance for Progress on the other hand failed because of lack of support from the receiving countries at least as much as from the creditor country. Some far too loosely described variant of such a body was proposed by the Netherlands delegation to the U.N. in 1966 and 1967 which called for a World Development Charter incorporating principles, directives and guidelines in the field of development cooperation and would provide a World Development Council to monitor fulfillment of obligations undertaken, progress made, requirements that are emerging and problems that need attention. The composition and functions of the World Development Council were then precisely described in a paper written for the Tinbergen Committee by Professor Max F. Millikan. ** - The difficulty of the World Development Charter idea is "that it could so easily become neither a spur nor a guideline but an exercise in futility, irrelevant to the real world of policy making." (R. Asher, op. cit., p. 98).

**Max F. Millikan, "Comments on a Procedure for Reporting and Evaluation of Development Progress during the Nineteen Seventies," E/AC.54/L.28, Tinbergen Committee, 1968.

Lastly, the system should provide balanced and impartial reviews of donor aid policies and programs from the standpoint of their contribution to development and the discharge of commitments undertaken." (p. 228/229).

But the precise methods of how to perform these functions are evaded. The Pearson report only recommends that the President of the World Bank should call a conference on that subject. It was probably difficult to find agreement among eight members of the Commission on such a delicate subject. Yet these questions are fundamental. They will be taken up in the second part of our report and exemplified in the case of Latin America.

3. The Prebisch Report*

i) The conclusions of all the reports are remarkably similar; they show that the theory and doctrine of development have crystallized in economics as well as in political economy. The impact of such reports, however depends not only on what is said, but on how it is said, on the sensitiveness, vibration and vigor of the message. The Prebisch report is in this respect an exception: it is a great manifesto of a great man. This, in spite of two shortcomings: a) a somewhat cavalier body of data; fortunately his conclusions stand up without having to rely on the implied econometric model b) while brilliant on what is to be done, the report is somewhat Don Quixotish on how it is to be done.

On two main points Prebisch offers new wine in old bottles:
a) the relation between the internal and external effort b) the relation between the rate of growth and employment.

[ad a)] Everybody stressed the point that the main development

task is that of the internal effort, which is to be supplemented by a marginal, albeit crucial, external effort. While that was more than a diplomatic formula at the beginning of the Alliance for Progress it soon degenerated into a mere lip-service. Interest in evaluation of programs and country studies was largely determined by the amount of aid it generated. Prebisch has here a new accent and new credibility. Development depends on both the internal and external effort; there were faults on both sides, and he stresses at least as much the fault on the internal front: insufficient capital formation and insufficient savings. Latin America was richer than other underdeveloped countries yet had no higher growth than the poorer countries. The increase in aid in the 1960's did not lead to an increase in national savings nor to a proportional increase in national investment. Insufficient external aid on the other hand failed to catalyze a potential increase in national savings and investment.

[ad b)] Everybody stresses nowadays that the objectives of development are not only growth of GNP, but also better income distribution, openness of society and notably that equality of opportunity which requires as a minimum full employment. The Prebisch report is here a seismographic apparatus sensitively registering social tremors. There is no stable solution in Latin America without a better income distribution, which is best realized by redistributing high increases in income, nor without full employment which can only be reached if a high ("internal") rate of growth is realized.

* Raul Prebisch: Transformacion y Desarollo, La Gran Tarea de America Latina, IDB, Washington, May 1970.

The new wine in the old bottle is the emphasis that Latin America confronts an "either-or" situation, that in fact it is at the crossroads: in order to achieve not only an increase in national income, but also full employment, which is a basic condition of equality of opportunity and social justice, a high rate of growth--around 8% (to be reached by 1980) according to Prebisch--is needed. There is no choice between doing a little less or a little more. To fulfill 90% of a target rate of growth may mean to fulfill only 50-60% of the target rate of employment. There are thus only three possibilities for underdeveloped countries: (a) A "distribution of poverty" sacrificing the increase in income for the sake of increasing employment; to have only a 3%-3.5% rate of growth (i.e., no increase in income per head) for the sake of creating a 3-3.5% increase in employment. This system would rely on large scale subsidies for small farms and handicrafts, subsidies which would absorb a great deal of savings which otherwise could be used for more productive output- and capital-creating activities. That would abandon hope for a noticeable increase in the standard of living, would lead to a series of mercantilist measures which would make a reinsertion into an integrated world economy (or even into regional Common Markets) impossible, but it would at least prevent a social explosion due to a rising unemployment. (That possibility is not mentioned by Prebisch; it is indeed the least probable). (b) To adopt a "compulsive" (communist) system, which, whatever its other great short-comings may be, at least provides for a high rate of growth and full employment. (c) To secure the achievement of a "critical

rate of growth," say 8%, which would lead to full employment ("sufficiencia dinamica") in a growing non-totalitarian economy.

ii) The 8% rate of growth is of course an order of magnitude; it may be different in different countries. A 6-6.5% rate of growth may absorb disguised unemployment in Chile, while a 7.5% rate may not do it in Colombia. This is basically correct and needed saying. Two problems arise, however: a) how reliable is the statistical and econometric demonstration; b) how to reach the high rate of growth?

[ad a)] The data on income distribution have a very high margin of error; notably the estimate of output per head of worker in agriculture being 27-28% of output per head of worker in non-agriculture seem to be out of line with similar estimates in the whole rest of the world. In most of the countries the output per head in agriculture varies between 40-50% of that of the worker outside. In Latin America industrial output may well be overestimated because of the high degree of protection. Even so income figures for agriculture seem to be underestimated. It is also a well-known phenomenon that as income per head increases, the percentage of manpower employed in agriculture falls. That will undoubtedly also happen in Latin America. But the results of a recent enquiry into the effects of the "green revolution" in the Punjab show that an increase in output of 100% led in spite of considerable mechanization to an increase in employment of 22%. Prebisch's conclusion, however, on the need for a "critical" high rate of growth as a condition of full employment seem to be confirmed by a

different method adopted in Italy where it was estimated in 1951* that only a 5-5.5% rate of growth (that seemed at least as "high" in 1951 as 8% seems today) can absorb within a decade the high open and disguised unemployment. The income multiplier of investment was assumed to be 1.8 while the employment multiplier was 1.23 in the short and 1.44 in the long run. These projections have been verified by results in the 1950's. A new series of estimates for over 40 sectors for different parts of the country show that over different three-year periods an increase of 1% in value added in different industrial sectors led to an increase in employment ranging from 0.17 to 0.28 only.** The conclusion of the Italian study in 1951 as well as now is that only a high rate of investment in efficient capital-intensive industries can lead to full employment at a rising standard of living.

iii) [ad b)] How is this high rate of growth to be reached? A high rate of investment with substantial increase in exports and new efficient import substitution is needed, which can only be reached if efforts at regional and subregional integration proceed far more successfully and quickly than they have done so far. Larger units of industry in a wider market can provide additional import substitution at efficient (lower) marginal costs which at the same time will enable many industries to be also competitive in exports to the world market. It is unlikely that the critical full employment rate of growth can be reached without integration. The message is: Grow and integrate or perish!

*The Effects of an Investment Program in the South of Italy, SVIMEZ, Rome, 1951 (both in Italian and separate English editions).

**See: Progetto Ottanta, Fetrinelli¹⁹⁶⁹ (Projections for the Italian Development Program 1970-1980).

In order to realize an 8% rate of growth national investment has to grow from 18% to 26.5% and national savings must rise from 14.5 to 24% i.e. by 70%! Even if we assume that during the first decade foreign capital inflow were to provide for 25% (and not 10% as foreseen for the decade of the 1980's) of total investment national savings would have to increase from 14.5% to 20% i.e. by 40%. They may have to rise even more to around 22% (i.e. by over 50%) if one half of the joint-venture foreign private investment ^{as agreed ex ante} /have to be taken/ over by national hands. That truly requires an extraordinary "discipline of development." If 60% of the population with its very low income is to be exempt both from taxation and savings it seems doubtful that savings and taxes on the 5% of the rich and 35% of middle-class incomes could yield sufficiently. A "discipline of development" that hard seems to be a somewhat "Don Quixotish" assumption. Either the absorption of the low income classes into the "modern" sector must take more than a decade, or other structural reforms--such as "forced savings" of say 10-15% from the increase in low wages and 20-25% from the increase in high wages to be invested by the working class in their own national investment trust (consisting of equities of national industries and constant purchasing power bonds)--should have been proposed. That seems to be the only way of securing an income redistribution without lowering the propensity to save (which is naturally lower among the low income classes).

The stupendous national effort has to be supplemented by a continuous and sufficient external aid which must be higher during the first decade of the 1970's to enable Latin America to restructure her economy, increase

national savings , investment and exports. Prebisch estimates that Latin America should continue to receive 15% of total aid to underdeveloped countries (suitably enlarged according to the UNCTAD and Pearson Committee postulates) as it had in the past. The future loans should all carry a 4% amortization rate, which is suitable for official lending, and either a 2% or a 6% rate of interest. An assumption of 2/3 of loans at 6% and one third of soft loans at 2% at a combined rate of 4.7% might appear to be more realistic. If the flow of official long-term lending is sufficient it may be expected that the proportion of short- and medium-term sellers credits would finally be suitably reduced. Over and above the 15% of total world aid a debt conversion for the presently existing indebtedness is proposed. It will undoubtedly be needed, but it is essentially an additional part of aid. Other parts of the underdeveloped world will also require it but Latin America's share is higher than that of the others. Debt conversion must be considered as an inherent part of total aid allocation, so as not to penalize those countries which did not indebt themselves to the same extent. More aid on expectation of more internal effort is an act of faith. On the opening meeting of the Committee of Nine they replied to a question on how they would proceed with their evaluation: "We shall be Catholic as to the past and Protestant as to the future." Let us start again.

The Prebisch report starts by describing facts (unemployment, bad income distribution, insufficient growth), continues to examine what should be done about it, and concludes that one way or another it will be

done. His is an appeal that it should be done by a peaceful revolution, by rational not irrational methods. It is a manifesto, a clarion call to the reasonableness of man not heard since the beginning of the Alliance for Progress nine years ago.

II. What Can Be Done About Latin American Development

1). Decline and Fall of the Alliance for Progress¹

The Alliance for Progress was the most complete and the most articulate manifesto of the development creed of our generation. But while it incorporates the most up-to-date thinking on social and economic development and could be both a program and a faith--the faith has evaporated. There is a lack of drive, mystique and élan which could compel public opinion to overcome the normal inertia and resistance to change. A peaceful revolution is more difficult than a violent one. All people have a "sentimiento tragico de la vida," they are prepared to die on the barricades but cannot mobilize enthusiasm for the middle way, for common sense, for a gradually better living. "Es cierto que el esfuerzo de desarrollo envuelve actividades que carecen del matiz heroico de una guerra. A la dirigencia nacional corresponde la tarea de proveer la inspiracion necesaria para imbuir a toda la nacion del espíritu de urgencia y de epopeya necesaria para librar con éxito esta guerra contra la miseria que es la Alianza para el Progreso."² It is difficult to create enthusiasm for a peaceful revolution, and this is the main task of Latin American leadership--but it is not impossible. The New Deal, the Marshall Plan, the Anglo-Scandinavian Socialism and Full Employment Welfare State, the development myopic in Nehru's India, the euphoria in the Kennedy days in the U.S. show that it can be achieved. It is conspicuously missing today.

¹ See: P.N. Rosenstein-Rodan: La Marcha de la Alianza para el Progreso, Progresso (Vision) 1966; Raul Saez: The Nine Wise Men and the Alliance for Progress, in Global Partnership (op. cit.) 1968; and, A.F. Lowenthal: Alliance Rhetoric versus Latin American Reality, Foreign Affairs, April 1970.

² El Futuro del Desarrollo de la America Latina y la Alianza para el Progreso, CIES/847, p. 324, (1968).

The Alliance for Progress failed because of sins of omission: neither of the two sides, /Latin America or U.S. governments have fulfilled their obligations. Most Latin American countries forgot the multilateral principle agreed upon in a euphoria of Punta del Este and the U.S. all too willingly complied with their wishes. The Alliance was more and more considered as a way of obtaining aid and not as an inherent part of an integrated development task; not as a catalyst, but sometimes as a substitute for national effort. To obtain more aid seemed easier and more familiar in bilateral talks. The U.S. on the other hand--without failing to implement in practice most of the recommendations referring to aid--did so consistently on the explicitly and exclusively articulated basis of its own evaluation in the form of a strictly bilateral negotiation. Bureaucracies on both sides, drowning in day-to-day problems, interpreted their role as having to adjust to reality" (i.e., to one-year's horizon) the lofty principles (i.e., a ten-year outlook) of the charter of Punta del Este. La Trahison des clercs created a vacuum between one-year's practice and ten-year vision.

While the Alliance for Progress failed, it is important to realize that it failed because of a lack of implementation, not because of faulty objectives. The philosophy and objectives, which incorporated the main Latin American ideals and ideas, are as valid as ever. When considering future policy it is the implementation of this program, not its content, which has to be radically changed.

Alberto Lleras Camargo¹ was right in stating: "The present situation will certainly change. No nation can afford the luxury of

¹Vision, 1965

maintaining for long an international policy of frustration. And before one starts talking of changing this policy with a different headline and different mottoes, one will discover that the Alliance for Progress is the one ~~secure~~ approach to the grave economic problem of Latin America and the only solution to social unrest in that part of the world. It is still possible to save it. But we have to return to its inception, its commitment and its spirit. That means to the brilliant moment of its proclamation. Before bureaucracy converts it into that we see today."

The Alliance for Progress will have to be rebuilt soberly and rationally without its initial short-lived elan (can one fall in love twice?), but with a genuine sense of urgency, not the complacency and disappointment /at present.
that mark it

The program of the Alliance was essentially Latin-American in its origin, but it had the Kennedy effervescence and style in its formulation. "The intellectual fashion is turning against (it) regarding the new frontier as at best empty rhetoric and at worst a kind of treacherous capitalist gradualism. The Kennedy era worked with energy adaptability and an invincible infectious optimism. It learned from its mistakes and went on believing and convincing other people that human ingenuity and good will can conquer many, if not all, obstacles."¹ In a different style of "low profile" the same content has to be reconstructed, otherwise "there is a risk, that new perceptions may become distorted because of a tendency to overcorrect for past errors. U.S. policies for the 1970's may come to be based on premises as inadequate, albeit in different directions, as those which underlay the Alliance. To become a less obtrusive and domineering

¹ D. Watt, in Observer, 28 June 1970

partner is one thing; to reduce our real interest in the common enterprise of inter-American development would be quite another. Further consideration suggests that there may be both more reason for concern and more cause for hope about Latin America than is currently realized. (p. 501) President Nixon's emphasis on the importance of Latin American initiatives and on the U.S. desire to be a partner is certainly salutary, as long as American actions demonstrate soon that the President's words were not merely a euphemism or a cover for U.S. inaction (p. 502). The challenge of the 1970's, for the United States and for Latin America, should be not to abandon the Alliance, but to forge a real one." (p. 508)²

Latin America also must mobilize Prebisch's "discipline of development" if the Alliance goals, which are Latin American goals, are to be met.

There are five main tasks for rebuilding the Alliance for Progress:

- i) To organize a constructive dialogue between the U.S. and Latin America; (see 2)
- ii) To multilateralize aid decisions, agreeing on principles ("criteria") of allocation of aid based on a functional independent evaluation of national and international development effort. (see 3)
- iii) Agreement on trade policy, the respective roles of trade and aid, and on methods to resolve conflicts. (see 4)
- iv) Agreement on regional and subregional integration (see 5)

²A.F. Lowenthal, op. cit, Foreign Affairs, April 1970.

- v) Agreement on principles of conduct in the field of private international investment. (see 6)

2. How to Organize a Dialogue

To change radically the implementation of what was the Alliance for Progress requires a serious dialogue between the U.S. and Latin America^{Cooperation between them} is not only, and not even, primarily an economic problem. It is a psychological and political problem. Most interdisciplinary problems appear in the form of one equation and two unknowns. But the relation between the U.S. and Latin America can be described as two unknowns without even one equation. One unknown is the U.S.-Latin American policy. The truth is that it does not exist. There are various wings of opinion in the U.S. administration and varying waves of attitudes, but a consistent U.S. policy towards Latin America is nonexistent. It is an anthropomorphic simplification and abstraction. Neither, however, does "Latin America" exist; it is also largely an abstract figure of speech. There are twenty different countries at different stages of the search for their national identity with less cohesive positive "Latin American wavelength" than was true of the "Pan-European idea," although more than is true of the "Asian cooperation." A common Latin American platform is not yet established. The OAS is a ponderous organization difficult to live with and impossible to live without. Neither OAS, nor CIAP, nor BID, or CEPAL can be as yet said to have a recognized mandate to speak in the name of Latin America. Perhaps the most valuable contribution of the U.S. to the Inter-American system is the fact that its presence constitutes the only common link between Latin American

countries: the common resentment of the U.S.; without which the relations between them would be even worse than they are today.

The structure of regional institutions is less important than the quality of men in them. A less functional organization with first class men will work better than an optimal "organogram" with lesser men. Post-war idealism aroused an enthusiastic cooperation between the U.S. and Europe in the Marshall Plan days. The best minds and people on both sides participated in its administration. There is distinctly less vibration in this field today. True, the reconstruction was an easier and shorter task than construction (development). It is also true that Europe had ampler human resources than Latin America where the best men are often needed at home and cannot be spared for missions abroad. Yet partnership for development requires full-time (or at worst full-half-time) people with a true national mandate and a sense of mission. The main obstacle resulting from international relations is the double difficulty of establishing a Latin American voice on the one hand, and a consistent (not vacillating) U.S. policy on the other hand, so as to organize a new constructive dialogue between partners in development.

The process of building a national sense of identity is not just a matter of creating institutions. It is a conscious assertion of the things which separate the nation (or region) from others. In this sense the CECLA consensus of Vina del Mar is a modest first step of self-assertion. But it is only a list of largely justified grievances and postulates of what the U.S. should do. It is thus a second act of a play in two acts without an indication in the first act of what Latin American governments intend to do.

A revived Alliance for Progress must establish such a common Latin American platform in the near future.

3. The need for an independent multilateral evaluation of development effort has been proclaimed already in 1954¹ by a group of experts set up by ECLA; it has been incorporated--albeit imperfectly--in the Charter of Punta del Este and is now being paid lip-service again in the generally proposed shift toward multilateralism (see I.2.XII and XIII).

Multilateralization was the basic principle of the Alliance for Progress. Its meaning does not refer primarily to: (a) targets; (b) projects (including even multinational projects); or (c) the forms of administration (national or multinational) but fundamentally to the spirit in which policy is operated, and the delegation of decisions on how to allocate aid, relying on evaluation of development programs by an independent multinational body.

While targets have been commonly proclaimed to consist of three main groups: (a) rate of growth; (b) improved income distribution and social progress; (c) achievement of these targets within the framework of an open society with evolutionary democratic methods--the relative importance or weight attached to each of these aims, which in the short run are largely conflicting with each other, is strictly national (not international) responsibility. Any progress in achieving those targets (for instance, an increase in investment represented by an additional investment project) is of national responsibility but of multinational concern. The evaluation of the national effort to achieve progress in the achievement of

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<sup>1</sup>"International Co-operation in a Latin American Development Policy" (E/CN.12/359).

those targets is a multilateral function implying the separation of financing and programming.

"The primary criterion for allocating aid is to maximize additional effort, not to maximize income created per dollar of aid. There is a natural credibility gap whether such a primary criterion will in fact be applied. Justified or unjustified suspicion that aid-giving might be used to obtain other concessions, that it will be subject to political or economic strings, impedes discussions of what measures are needed and are possible to increase or to optimize national effort. The incentive effect of aid as a catalyst of (and not a substitute for) often painful and difficult national development measures is weakened. The very discussion by a credit-giving country of what the receiving country should do invariably raises objections that the latter's national sovereignty is being infringed. Under such circumstances, the discussion is either incomplete and not explicitly articulated or it is bound to give rise to bad blood and mutual recrimination. In practice, both effects occur in a varying mix of disadvantages. It is natural, therefore, that from time to time, there have been in the post-war years demands for the establishment of procedures for an independent evaluation of national development efforts, the results of which would be acceptable to both the donors and the recipients of aid. An impartial international evaluation is an attempt to reconcile the legitimate interests of both parties, avoiding thereby the friction that could result from potential differences of opinion between them."<sup>2</sup>

Three questions arise in this context: i) What are the criteria of

<sup>2</sup> "A Study on Independent International Evaluation of National Development Efforts," UNCTAD, TD/7/ Supp. 15, 11 December 1967.

evaluation? ii) Can they be applied without interfering in national sovereignty? iii) Who should apply them?

i) Criteria of Evaluation. If national development efforts of countries could not be measured, assessed or estimated, aid could not be allocated to different countries according to a coherent principle. An evaluation of national development effort presupposes the existence of operational criteria which could be applied in practice to determine the amount of aid required. Such criteria--although approximate and subject to high margins of error do exist and can be applied to yield at least a rough assessment ("sufficient" or "insufficient") or ranking of national effort.

There are three main difficulties in reaching "measurement" (not "only assessment) of national effort.<sup>3</sup> First, national development objectives consist not only in the rate of growth but also in better income distribution (including notably full employment) and other social goals. These objectives cannot be just listed qualitatively; they are often in conflict with each other; more of one can only be obtained at the expense of less of the other.

Second, an intertemporal choice has to be made of how quickly, and how much of each objective is to be reached over successive time periods. If there were only one objective (for instance national income) to be maximized over one period of time, national effort could be measured exactly. If there were only one objective to be optimized over several time periods (the present generation's consumption is also a part of welfare) efforts of different nations could be ranked ("first, second, third, etc."). If there are, however, several groups of objectives to be met over several time

<sup>3</sup> For a more detailed discussion see the author's: Criteria for Evaluation of National Development Effort, Journal of Development Planning, No. 1, 1969.

periods only a dichotomous classification ('pass or fail') is possible. Even that is a sufficient basis for decisions if the sum total of allocated aid to those countries whose effort is "adequate" were available. No comparative measurement that one country's effort is 25% higher than that of another country is implied, nor is it necessary. Only if the total amount of available international aid were insufficient, if it amounted f.i. to only 0.5% instead of 0.75% of developed nations GNP a proportional cut of 33% aid to each country would not be warranted. Countries with a higher national effort should have a smaller and those with a lower national effort a higher cut in aid. Such a handling of aid deficit would require a ranking of propensities of national effort. Such a ranking is still in the nature of an informed guess. Only a "second best" allocation of aid is possible under these circumstances and it may be very inferior to the optimal one.

The very fact of the criteria for evaluation of national effort being tentative, approximate and subject to high margins of error makes it important that there should be full confidence that such functional impartial criteria are being applied. A credibility gap would weaken the incentive effect of aid towards additional national effort. An impartial international evaluation should, therefore, prevail. Rough as they are, evaluation criteria do not become any better if they are applied, or are said to be applied, by national instead of international agencies. The very fact that only rough approximations, rather than exact measurements of national efforts are possible, far from being an argument against delegating such

judgments, is an argument for an independent and multilateral evaluation.<sup>4</sup>

The third difficulty in evaluating national efforts, apart from the deficiencies of statistical data, stems from the loose and indeterminate nature of each country's system of objectives, in other words, its "social welfare function."<sup>5</sup> The rationalist's assumption that people know what they want is as unrealistic as the assumption that they think before they act. National planning reveals these social values. It is a method that provides additional information not only about means but also about ends which normal market mechanism cannot provide. It thus makes for a more rational policy and for a "democratic" interpretation of people's wants. If the relative factor weights of the different ultimate aims, including their trade-offs, were determined, the countries' efforts in achieving them could be estimated and compared. Since the means to achieve these objectives are not certain, especially in the social sphere, the strategy of social development being still more indeterminate than that of economic development, the development efforts may not be comparable but only capable of dichotomous classification, to determine which efforts are adequate.

ii) Method of evaluation without interfering in national sovereignty

National development objectives relate not only to a rate of growth but also to income distribution and other social goals. The economist is no more competent to make value judgments about them than any other citizen. The function of the economist is only to reveal explicitly the implication of

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<sup>4</sup> The problems and history of independent evaluations are described in the present author's A Study of Independent International Evaluation of National Development Efforts, United Nations Conference on Trade and Development (UNCTAD), td/7/Supp. 15, December 1967.

policy decisions and also the possible conflicts between various objectives. The nation then can make an informed choice. Aid, however, will be allocated within the wide but not unlimited area where the national objectives coincide with the international aid objectives. The international welfare function is an additional constraint on the national one.

An international evaluation has accordingly to proceed on two principles: both the nation's objectives and its preference by what mix of policy instruments they are to be reached should be taken as data. It is the nation's not the evaluators' value judgment which determines the goals of development. If the report were to find for instance that not enough is invested in social objectives (education, housing, health, etc.) then it can only point out that the allocation in the national development program does not correspond to the nation's proclaimed objectives. If, however, national aims give much greater weight to "economic" (growth of income) than to "social" objectives, then the evaluators have no right to propose changes. Only if a nation's social welfare function were clearly outside the boundaries of the international (aid) welfare function--i.e., if it consciously adopted a policy of "apres nous le deluge" without any increase in savings, investment or social betterment--can the evaluators decide to recommend no aid. Again, however, this international welfare function is often loose and imprecise. Many objectives of aid donors are often, consciously or unconsciously, not clearly articulated. International conscience, though not always international practice, is however, in full agreement on a large part of the rationale of aid. The developmental aim to accelerate the rate of

economic and social progress, or in other words, to contribute to an international equality of opportunity is generally accepted. Almost any combination of national objectives which does not imply too long a reliance on continued aid and too low an effort will be within the boundaries which the international welfare function imposes on the national one. The constraints imposed on the ultimate objectives of a nation by the rationale of international aid philosophy are thus not markedly restrictive in practice.

Conflicts arise more frequently only about the means how to achieve the ends. Once again national governments should have the say which combination of means they select to realize their ends. Some may prefer to give 75% weight to monetary and 25% to fiscal policy; some may prefer a different mix. Some may prefer more, some may prefer less controls. All the evaluators have to examine--and this is very much in practice--is whether the sum total of policy instruments is consistent and apt to have the proclaimed result. If for instance, a Government prefers to subsidize losses of municipal waterworks in a town rather than raise prices, then the evaluators can only point out that it might not be possible to implement the plan to have twenty such waterworks built during the next year; if the reply were to be (it seldom is) that subsidies will be provided for all twenty works then it is the government's right to choose its policy.

It may be only a semantic difference--but it makes all the difference how things are said.

iii) Who should be the evaluators?

a) The evaluation of development effort must be functional and

independent. It "must instill confidence in its wisdom, objectivity, technical competence, and independence of the special interests of particular donors or recipients...The evaluating body must have a membership which does not conceive of itself as representing the interests either of particular donor or recipient nations or of international bodies which have substantial funds to allocate for development purposes. This means that the members of this body should neither be officially designated by governments nor officially representative of either lending or claimant international institutions."<sup>1</sup>

The evaluating committee (whatever its name: Committee of Nine, or a regional sub-committee of a World Development Council, etc.) would have no legal sanctions or executive power behind it but would rely, like the International Court--on international good faith.<sup>2</sup> "Hopefully the reviewers of underdeveloped country plans will be of a quality and objectivity which will result in the review being taken very seriously by national and international agencies supplying resources for development in their own allocation of funds. While the Council is envisaged as a judicial and not an executive body and its recommendations will therefore have a purely advisory formal status, its effectiveness over time will inevitably depend on the influence which it turns out to have on both recipients and donors."<sup>3</sup>

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<sup>1</sup> Max F. Millikan: Comments on a Procedure for Reporting and Evaluation of Development Progress during the Nineteen Seventies (Tinbergen Committee) U.N. E/AC.54/L.28, April 1968. The author states that he is largely influenced by the program of the Alliance for Progress.

<sup>2</sup> The American Secretary of State Elihu Root, in fact introduced the proposed legislation of the U.S. adherence to the International Court in 1907 by saying: "It has been a general practice for arbitrators to act not as judges but as negotiators effecting settlements of the questions brought before them."

<sup>3</sup> Max F. Millikan, op. cit., p. 10.

Both receiving and donor countries must be prepared to delegate decisions on allocation and use of aid to such a "Committee of Wise Men." There are precedents of delegations of decisions de facto, and not de jure: for instance, the Council of Ministers pf OEEC under the Marshall Plan issued de jure recommendations but de facto decisions about how to allocate aid. On the other hand, neither Latin American or U.S. governments were in fact prepared to delegate decisions to the Committee of IX. Any delegation of decisions--like all progress in international relations--implies a limitation of national sovereignty. One of the sovereign rights is to accept the limitation of one's sovereignty. Most progress in history has just been proclaimed to be "impossible" only to be introduced de facto afterwards. We should not accept it as a datum that a delegation of aid decisions to a de facto sort of International Court of Justice is "impossible." An independent multilateral evaluation of development efforts is undoubtedly an optimum solution and should remain a not too long-run ideal. The influence of an only advisory body should not be underestimated. The Council of Economic Advisors in the U.S. has only an advisory function, but it creates a functional constraint. Even if the President rejects the advice, he has to take account of it, formulate his decision in non-political terms, thereby changing it in most cases in a functional direction.

In the transition towards a fully independent evaluation second- and third-best solutions may be envisaged in a non-perfectionist way--such as a discussion, persuasion, and negotiation on allocation and use of aid before a multilateral although not independent inter-governmental or inter-ministerial body. Discussions on such international bodies (example CIAP)

will always be necessary as a complement and essential sequence to an independent evaluation. They can be for some time--albeit imperfect--substitutes for the better solution.

There are two reasons why a not fully independent committee (i.e., one with government ~ or lending agency-appointed representatives) cannot offer a fully satisfactory solution. One is that it will not in practice fully remove the (justified or unjustified) suspicion of political strings attached to aid. The second reason is that there are parts of national development programs which do not lend themselves to semi-public discussions on intergovernmental platforms. Economic diplomacy like any other cannot be fully public.

b) Two kinds of evaluation: of an orientative and operative plan.

Any development program consists of an orientative long (5 or 10 years) term plan, and an operative plan considering how the orientative plan is to be implemented during the next year. The orientative plan incorporates the country's objectives (social welfare function) and the means proposed (both structural reforms and current policy instruments) to reach them. Those have to be evaluated according to the methodology described in the previous paragraph (3.ii). The evaluation procedure is necessarily a long process which involves not only a thorough study but also a series of discussions, suggestions, and de facto negotiations with the government about what tempo of structural reforms and of stepping up of national effort is possible. Such discussions are in practice impossible in a public hearing with all the national and international agencies present. Nor can motivations and

difficulties be openly discussed within the presence of other (either receiving or donor) governments. No religion prescribes an open confession of sins (at least when they can be listened to) and no marriage could survive if partners told each other not only what they are doing but also what at any time they are thinking of. Nor can all the details of such discussions be aired publicly after they have taken place. The value of the evaluation report by an independent body (which commands more confidence and thereby possibly more moral standing) does not consist primarily in its findings and conclusions, but in the procedure of arriving at them by a series of discussions between the government and a committee which does not represent either creditors or debtors. Such confidential discussions may enable the evaluating committee better to understand the country's problem and also enable the government to appreciate more the need for raising national effort. They will also make it clear, without causing as much resentment as would arise from discussion with government representatives, that the recommended amount, continuity and flexibility of aid will depend on what catalytic effect on mobilizing additional national effort aid can be expected to produce. A vital part of such discussions must necessarily take place behind closed doors, if it is to be fully useful. All the details of talks behind closed doors cannot be revealed to anybody, not even to CIAP. The plan reviews should not be conducted publicly but should be carried out at least in part by intimate consultation between the panel and the responsible officials of the host government so that the panel can acquire a full understanding of all the sensitive issues which enter into the domestic policy process of the government's questions. The plans finally resulting from those discussions

would of course, like most plans, be public documents.. Where analysis reveals discrepancies the panel could point them out and make either public or private recommendations as deemed in its judgment most wise as to ways to overcome them. This is obviously a sensitive area into which the council would have to move initially with some caution.<sup>1</sup>

In part, of course, such functions are attempted by missions of the IBRD or CIAP but they cannot go so far, nor can they be so readily accepted, because nobody can without considerable cost wear two hats at the same time: one of an independent evaluator and one of an operator who has to report to his agency or government.

Once the basic philosophy and technique of the orientative plan has been independently evaluated, progress reports and evaluations of the operative plan must be undertaken considering how the orientative plan is to be implemented during the next year. After one year has passed progress reports or country reviews have three tasks: a) compare and contrast the ex-ante projection with the ex-post realization; what were the discrepancies due to? b) elaborate the operative plan for the subsequent year; c) elaborate (or re-elaborate) the next stage of the orientative plan with one more year added, since an additional year entered the horizon of the 5 year plan.

Yearly country reviews which are progress reports and evaluations of the operative plan are thus a vital part of the evaluation process. They lend themselves admirably to the present procedure by CIAP which has several important advantages. They provide a platform for contact among all agencies.

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<sup>1</sup> Max F. Millikan, op. cit., p. 11.

Although none of them assume any obligation or commitment on financing, the meetings yield additional information and possibly on occasion suggestions of a different approach to diagnosis or prognosis. Not only capital-exporting but also capital-importing countries are present. Representatives of the country present and confronted with the evaluation have the knowledge that decisions are not taken behind their back and not without them being heard.

The implementation and negotiation of the orientative plan evaluated previously by an independent panel and common discussion and recommendations on the evaluation of an operative plan--which is an essential "monitoring" progress report--are and should remain the vital function of CIAP. An effective multilateral system could not function otherwise.

c) Co-ordination of various missions

Neither an independent evaluation panel nor C.I.A.P. has sufficient staff to perform all the necessary work. So far only the U.S.A.I.D. had country missions in all underdeveloped countries and the IERD is now expanding its already impressive series of country reports which in fact evaluate not only projects or sectors but also overall development performance and programs. "At the moment, the dynamism of the principal multilateral source of development assistance, the World Bank Group, stands in strong contrast to the weariness that has overtaken the major bilateral programs."<sup>\*</sup> It is obvious that other institutions should make use of the ample human resources of the World Bank and of regular country studies. It would be a waste to attempt and impossible to mobilize an additional staff to duplicate this

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<sup>\*</sup>R.E. Asher, "Development Assistance in the Seventies," Brookings Inst., Washington, D.C. 1970, p. 124.

effort. Moreover, an agreement how to participate in the World Bank missions is essential in order not only to make better use of them but also to avoid the too numerous missions, asking similar questions which create an excessive, intolerable and avoidable burden to high officials in the developing countries. While representatives of other agencies (IMF, CIAP, IDB) should participate in the IIRD missions it should be clearly understood that the World Bank reports only provide documentation and material for an evaluation of development efforts but have no mandate to determine a multilaterally committing recommendation on priorities use and allocation of aid from all sources. It cannot be the evaluation agency whose verdict should be accepted and followed by all the others for two reasons. First, because the voting power is in the majority that of the creditor not debtor countries. While the management of the IIRD is largely independent this may change any time; this creates a credibility gap in the underdeveloped countries. Caesar's wife must not only be virtuous but must also be above suspicion. Secondly, the staff members of the Bank who evaluate the development effort also take part in loan negotiations, so that they are both judges and executors at the same time. While money commands respect, it also creates resentment and suspicion. "It is important on the one hand to concentrate resources at a point at which some leadership and leverage can be exercised and on the other hand not to give any agency a monopoly position or delusions of grandeur...Less developed countries are no more eager to become wards of the World Bank or the United Nations than of the United States or the U.S.S.R."\*\*

\* R.E. Asher, op. cit., pp. 128 and 129.

In Latin America the IDB and IIRD are at present supplying almost two-thirds of aid. Many a criticism levied against the U.S. may soon be redirected towards them. An independent multilateral evaluating body may also be criticized by both sides as a predominance of technocracy or bureaucracy. Yet the very fact that they do not represent governments or "money," that they act in a form which neatly separates programming from financing will make their verdict more acceptable even if not always welcome.

While staff members of other agencies should participate in the missions, they are not committed to the IIRD conclusions. There should be one mission but several reports; each agency's representatives can formulate their own evaluation. The confrontation of different evaluations will be useful and stimulating to all participants. It will reveal what different conclusions are due to and thereby improve the subsequent analysis.

"One mission, several reports" seems to us to be a better formula than the Prebisch report proposal (pp. 147-149) to include representation of international lending agencies and of Governments through DAC in the group of experts who are to evaluate the development effort.<sup>1)</sup> Information can be obtained by the participation of staff members of the group of experts in the common mission. Participants in that mission should not be confined to representation of international lending agencies; national lending agencies (for instance, A.I.D. from the U.S.) should also be on it; it is not enough to have the bilateral lenders represented by DAC, whose staff members cannot commit the national lending agencies even to a merely technical judgment.

The group of experts would better preserve its image of an

1) The evaluation of the Group of Experts and of CIAP would be primarily concerned with the allocation of aid, not with project analysis and selection.

"independent court" if it were autonomous. Apart from evaluating the orientative plans, they should also participate--like representatives of other agencies--in the evaluation of operative plans and progress reports received within CIAP.

An autonomous group of experts could then evolve into a Sub-Committee of a World Development Council to be established under the U.N. \* which could best function through several regional sub-committees. Latin America is only one part of the underdeveloped world. Aid should be allocated to all of them according to functional criteria. Before such a World Development Council is appointed CIAP as well as the Group of Experts should keep account of the equitable distribution of world aid when it presents its estimate of external resources required for Latin American development.

Trade and Aid: <sup>1</sup> An Ombudsman on Trade Policy Conflicts?

To a large extent, trade and aid are substitutes for each other. Varying proportions of trade concessions and aid can be envisaged remembering that normally one dollar of aid is an equivalent of around four dollars of trade, since resource costs of exports amount to 70-75% and profits to 25-30%. In the shorter run in which the foreign exchange gap is larger than the resources gap, these proportions may be different; one dollar of aid

\* Since we only deal with problems of Latin America we do/<sup>not</sup> enter into the discussion of various possible forms of establishing a 'World Development Council' or "An International Commission on Development." A set of papers on "An International System of Development : Issues and Alternative Approaches" has been prepared and discussed at the Heidelberg meeting in June 1970 following the informal meeting held at Montebello in February 1970 after the Columbia University meeting on the Pearson report.

<sup>1</sup> For a more detailed discussion, see I 2 XII.

may be an equivalent of only two or two and a half dollars of trade, which implies for the shorter run a shadow rate of foreign exchange up to 40-100% higher than the nominal rate of exchange. This is the reason why non-reciprocal tariff preferences for underdeveloped countries should be introduced for a certain period, say for a decade, with an annual reduction of these preferences by 10% each year in the following decade. That would apply a policy of a sort of international infant industry protection with a defined period of infancy.

Abolition of quotas and trade restrictions may be more valuable than non-reciprocal preferences on industrial products. A committee to negotiate conflicts on trade between the U.S. and Latin America has now been created. International trade should of course be considered as an inherent part of development assistance, not as a separate chapter. If the relation between the U.S. and Latin America is truly to be a partnership of the Alliance for Progress, arbitration on conflicts should be agreed upon. This is vital for CIAP (not the independent Group of Experts) activity. It might be rendered easier if within the Inter-American System connected with CIAP an office of a Western Hemisphere Ombudsman were created.<sup>1)</sup> It would pronounce on violations of the spirit of cooperation in development not only between U.S. and Latin American countries, but also on "bad" practices between Latin American countries. The great difficulty--apart from limiting the freedom of action of each country--is a lack of consensus on standards to be applied. The ombudsman in any system is a guarantee of legality, which implies a given system of law. You know what you are supposed to apply. An agreed set of economic values in matters of international trade policy does not yet

1) Negotiation and possibly arbitration of conflicts must precede any function of the Ombudsman.

exist although GATT and UNCTAD move in that direction. An Ombudsman would have to act in a spirit of Common Law in process of creation, not of a formal Roman Law principle. He could point out where there are certain inconsistencies between the professed doctrine and reality.

The most valuable preferences and steps towards liberalization of international trade--in the field of agricultural products (grains, butter, cheese, and meat) and of textiles--will be most difficult to obtain. This is a reason why aid has to continue for a longer period than would otherwise be necessary. But liberalization of trade in other manufacturing industries will offer a growing potential of exports to underdeveloped countries. When income per head and wages rise, normal principles of international division of labor should lead to increasing imports of labor intensive products to developed countries.

The most important progress in both increasing the international trade and accelerating and strengthening economic development, however, would be the economic integration of Latin America.

5) Economic Integration<sup>1</sup>

i) Economic integration of Latin America is the condition sine qua non of a sustained high rate of growth, of economic independence and of a heard voice in the concert of world policy. The widening of the market would lead to the creation of optimum dimensions in industrial sectors. This would not only create a vast additional scope for an efficient import substitution,

<sup>1</sup> The text largely follows the author's: "Obstacles to Change from International Relations" (Part VI). A report presented at the Conference of the Center for the Study of Democratic Institutions, Mexico City, Sept. 1969; included in the publication of the Center: One Spark from Holocaust.

but also increase the export potential to the world market. Once optimum dimensions are reached, firms would be competitive not only for inter-Latin American, but also for international trade. Perfectionism trying at once to establish a complete economic union harmonizing all economic policies is the main danger here. After twelve years this has not been accomplished in the European Common Market, which nonetheless is a conspicuous success. The better (a complete economic union) may be the enemy of the most essential good (automatic tariff reduction). It is true that there are great difficulties of transition towards such a Common Market, amply discussed in economic literature. But the advantages are so great that the difficult task should be undertaken. While no responsible voice can openly deny it, we are nowhere near the realization of this program. Rather than to belabor the obvious in describing the advantages of economic integration, let us examine the reasons why only lip service of platonic ideals, but no effective steps to realize them are taken.

ii) The difficulties in the formation of the European Common Market are a useful analogy for the Latin American situation. Four fears constituted the main obstacles to the formation of the Common Market; in varying proportions, the same fears prevent progress in Latin America.

a. The fear of the industrialists not to be competitive under a system of gradual, but automatic tariff reduction. This cannot be true for all firms, but the industrialists do not and did not behave in a logically consistent way. Most associations of industrialists (Comité des Forges, Confindustria, etc.) in Europe, like those today in Latin America, vigorously

opposed the formation of the Common Market. If it was formed nonetheless, this was due to the decision of four great statesmen in Europe, Jean Monnet, Schumann, Adenauer and De Gasperi, to overrule the opposition of the industrialists. No analogy is as yet in sight in Latin America.

b. The fear that the requirements of competitiveness will stop or weaken social progress and better income distribution was widespread in socialist and left wing quarters. It was the main reason for the Labor Government in England to refuse to join the ECM--in fact the higher rate of growth in the ECM enabled both social and economic progress. Social progress from an admittedly lower basis was greater in the ECM than in England. This fear does not seem to be as vividly articulated in Latin America as it was in Europe.

c. The fear that countries of lesser development (like Italy in Europe) will not benefit or benefit less from economic integration whose main advantages will accrue to the more developed countries. This fear is widespread in Latin America. Special provisions for countries of lower development level are foreseen. Even if the principles are not always clearly or logically formulated--the application of privileges is facilitated by the fact that such countries only form<sup>4-5%</sup> of the G.N.P. of Latin America.

d. The fear that under the umbrella of regional preference international corporations (largely U.S.) will take better advantage of the new opportunities than national investors, is widespread in Latin America. After all, the purpose of economic integration is not to offer advantages to foreign investors. This fear was not present at the beginning of the European

Common Market, but it emerged in recent years in a much stronger form. An agreement on how to regulate private international investment is vital in order to remove the fourth fear which is one of the main obstacles to economic integration. We shall discuss this problem area forthwith. (VI).

iii) If an agreement among six countries to form the European Common Market was so difficult--it was in fact a matter of "touch and go"--there is no wonder that an agreement among twenty Latin American countries is infinitely more difficult. It is in fact not probable during the next decade in spite of all the pious declarations of intent. The only practical way seems to be to reach agreement among smaller groups of four, five or six countries and to proceed to form several "Latin American Beneluxes." Benelux preceded the formation of the European Common Market and was no obstacle to its creation. Even the formation of regional subgroups of proper size may be hindered in the case of countries with very different levels of tariffs. It might be worth while to consider the formation of such subgroups in two stages as well: during the first five years (say, 1971-76) tariffs would be automatically reduced from whatever their levels are; a common external tariff would only be introduced in the subsequent decade (say, 1977-1987).

Economic integration would proceed in three stages: first, automatic reduction of existing tariff levels in regional subgroupings; second, establishment of common external tariff within regional subgrouping; third, integration of the regional subgroups into a Latin American Common Market.

## VI. Agreement on Practice and Conduct of Private International Investment

This is one of the most important and urgent tasks of international cooperation. The fear of economic foreign domination is a serious obstacle to economic integration and to good international relations. The fears may be exaggerated, the arguments on both sides may be emotionally loaded, but this in itself is a ground for a sober analysis of that problem area. The fears are moreover so widespread that, in spite of frequently loose and inexact articulation, they cannot be dismissed as mere hysterical nationalism. Where there is so much smoke, there is some fire.

Lawyers are even more conservative than economists. The rules of conduct in private international investment have been formulated a century ago in the commercial law. At that time they may even have represented an area of mutual interest. International investment is undoubtedly on balance beneficial to both the investing and receiving countries, but the topography of the area of mutual interest is different today from what it was a century ago. New rules should be agreed upon based on today's economic structure and reality. The set of problems arising from private international investment has been examined systematically in CIAP papers and at the round table at the meeting of the board of governors of I.D.B. at Bogota in April, 1968.

An agreement should be negotiated not in a spirit of animosity but in an endeavor to define the new basis of mutual interest which would reduce risks and would create a favorable climate for foreign investment. The agreement should refer only to prospective investments, not to the stock of existing ones. If Latin American countries for various reasons do not

Wish to agree to the arbitration settlement of disputes under the aegis of the IBRD they should create an arbitration forum of the Latin American system possibly with IDB and CIAP.

Private International investment brings seven contributions to development:

- i) it helps to close the "resources (savings) gap";
- ii) it helps to close the "foreign exchange gap" (long-term bonds, when available, can offer these two contributions more cheaply); ..
- iii) it helps to overcome the "managerial gap;"
- iv) it helps to close the "technological gap;"
- v) it contributes to close the "commercialization (foreign trade) gap;"
- vi) it contributes (positively on balance, but also negatively) to the formation of national entrepreneurship
- vii) (Negative effect), unless agreed controls are applied it may weaken the control of national economic policy by transferring the center of decisions abroad.

A cost-benefit ratio applied to these seven functions would answer three questions:

- a) does that form of investment in a given sector or project cost too much?
- b) What effect has it on the formation of national entrepreneurship (positive through national managers in foreign subsidiaries, through the demonstration effect on management, through sub-contracts which create new

investment opportunities negative through buying up existing enterprises and stifling "infant entrepreneurship.")

c) to what extent does it weaken national control of economic policy decisions?

According to cost-benefit analysis of this type, governments will announce which sectors have a high, medium or low priority for prospective foreign investment.

Private international investment is a valuable and unsubstitutable complement of aid, but it cannot solve the development problem alone. only if a proper proportion of aid be forthcoming--say 60-65% in higher income, and 65-75% in lower income underdeveloped countries--can private investment effectively contribute to the "harmony of interests" of both sides. But its form and modality must change. Irrevocable options to sell 50% or the majority of shares to national hands after a certain time (varying from say 7 to 12 years in different sectors) will lead to the prevalence of joint ventures; the attitude will change; what is foreign investment today will be in the majority national investment tomorrow. Far from being met with hostility it will be unambiguously welcome, which will facilitate international cooperation, reduce risks and benefit both sides. But in order to remove the obstacle resulting from international relations, agreement must be reached on two levels first, among the Latin American countries, to apply identical principles rather than to compete with each other, by granting better conditions so as to attract more international investment second, among Latin American receiving and the developed investing countries so that the rules for future foreign investment be clearly known and do not give rise to conflicts and misunderstandings in the future.

7) Programming of internal and external resources for development.

a) Aid is only a supplement to total national development effort, not to single parts of it (projects), hence the need for programming, within each nation's development plan, of all available (internal and external) resources. Partnership and cooperation by creditor countries has to be considered in its total composition (i.e., programmed), since its contribution consists not only of external resources of aid, but also of trade and investment policy. The four contributions by 1) aid, 2) trade policy including tariff preferences, 3) commodity agreements buffer-stocks and supplementary finance and 4) debt conversion should be part of a coherent whole. They can within wide limits substitutes be for each other. When estimating external source requirements CIAP should study the "efficiency units" and "rates of substitution" of these four contributions to the development effort.

b) Debt conversion operations are an urgent necessity in view of the level and structure of foreign indebtedness in many underdeveloped countries. In 1964 already it was stated at the CIES conference in Mexico that "debt conversion has become an imperative chapter in international aid policy." At present CIAP, IBRD and other institutions are studying the problem.<sup>1</sup> Since the need for conversion is widespread one should not 'deal with each case

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<sup>1</sup>An excellent exposition and analysis is given by: D. Avramovic, Latin American External Debt: A Study in Resource Plans and in Terms of Borrowing, IBRD, August 1969. See also Ch. R. Frank, Jr., Debt and Terms of Aid, Overseas Development Council, 1970

as and when it arises" or "on its merit." Some general principles can be stated; there is a dilemma, however, how to deal with some others:

- 1) Debt conversion represents additional financing and should be counted as a grant of external resources. It is a particularly valuable part of aid since it is in fact an untied program loan. While it presents many difficulties, it may be easy to obtain for legal and institutional reasons.
- 2) Countries which are less indebted than other should not be penalized. Debt conversion should not create a negative incentive. It will not, if it is counted as part of general aid. Countries with lower indebtedness should get more aid.
- 3) It can be assumed in most cases that the foreign exchange gap is only greater than the resources gap over a medium term of five to ten years. A good development policy should reduce or abolish the excess of the foreign exchange gap by diversification and increase of exports and by an efficient additional import substitution. Where the "bunching" of repayments is mainly concentrated over the next 2-3 years the "hump" can be more easily overcome.
- 4) Conversion action should be undertaken on similar lines by different creditor countries--otherwise financing by one country could in fact be used for repaying another country. Care should also be taken that conversion of loans of longer maturity should not lead to repayment and recontracting of additional short-term debt.
- 5) Debt conversion is part of total aid policy. It may improve the country's credit worthiness--but without receiving sufficient capital inflow for development it would not solve the problem. One either supplies enough finance for development as well as repayment or one might as well face default. Nor does it make sense to say: "Let us first put the house in financial order and grant aid afterwards." Only if sufficient capital is made available can financial order be restored without endangering development. As in all aid policy, an act of faith is required that development effort and policy will be better in the future than it was in the past.

There is a dilemma, however, how far one should pass judgment on what the excessive indebtedness is due to. In some cases countries borrowed to finance consumption and capital flight. The inflow of capital did not lead to higher investment. In other cases, borrowed foreign funds went into

investment in spite of monetary and financial disorder. Excessive borrowing of short term exporters credits may have been the cause of trouble in some countries, but not in others. Lack of adequate supply of long-term credit may have been the reason for excessive short-term borrowing--after all a man who is drowning will reach for a shark's tail in order not to sink--but financial light-headedness may have been the overwhelming reason in other cases. Should one treat both cases alike, thereby "rewarding" less stringent policies, or let bygones be bygones? It is written in the Bible that sons pay for the sins of their fathers, but investigating the country's responsibility for the debt payments difficulty cannot be pushed too far in a fruitful way. If there are reasonable prospects for a better national effort in the future a double act of faith in offering debt conversion and aid for development under strict conditions may be the path of wisdom.

8) Conclusion

The agenda is formidable. A strengthened Alliance for Progress organization consisting of CIAP, the Group of Experts, IDB, the Ombudsman for Trade Problems, and a Latin American Center for Arbitration of Investment Disputes can deal with it if a new spirit of partnership in development is to arise. As soon as it is seen or believed that the challenge is being met the best men in Latin America will join the ranks. Today the system is defended from attack <sup>/of</sup> in the spirit "*klein aber mein*" (little but mine!). This is only a negative defensive attitude. It can become positive and constructive. Latin America can solve her development problem--however difficult--sooner (within a generation) than other underdeveloped areas of the world.







